

# **CITY OF ANNAPOLIS, MARYLAND**

## **Notes to Basic Financial Statements**

June 30, 2003

### **(1) Summary of Significant Accounting Policies**

The City of Annapolis (City) is an incorporated municipality governed by a mayor and eight aldermen who together constitute the City Council. The City government provides most basic local governmental services except education, which is provided through the Anne Arundel County Board of Education.

For financial reporting purposes, the basic financial statements include the various departments governed directly by the City Council. The City does not have any component units as defined by generally accepted accounting principles. The Mayor is responsible for appointing the commissioners of the Annapolis Public Housing Authority, but the City's accountability for this organization does not extend beyond making the appointment.

The accounting policies of the City conform to generally accepted accounting principles (GAAP) as applicable to governmental units. The following is a summary of the more significant policies:

#### **(A) Basis of Presentation - Fund Accounting**

The accounting system is organized and operated on a fund basis. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations.

The City's funds are grouped into two broad fund categories and five generic fund types for financial statement presentation purposes. Governmental funds include the general, special revenue and capital projects funds. Proprietary funds include enterprise funds and an internal service fund. The City has one fiduciary agency fund.

#### **(B) Basis of Accounting**

### **GOVERNMENT-WIDE FINANCIAL STATEMENTS**

The government-wide financial statements (i.e., the Statement of Net Assets and the Statement of Activities) report information on all non-fiduciary activities of the primary government. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which primarily rely on fees and charges for support. Internal service fund activity is eliminated to avoid "doubling up" revenues and expenses. Fiduciary funds are excluded from the government-wide financial statements.

The government-wide statements are prepared using the economic resources measurement focus and the accrual basis of accounting. This is the same approach used in the preparation of the proprietary fund financial statements but differs from the manner in which governmental fund financial statements are prepared. Therefore, governmental fund financial statements include reconciliations with brief explanations to better identify the relationship between the government-wide statements and the statements for governmental funds. The primary effect of internal activity has been eliminated from the government-wide financial statements.

## **CITY OF ANNAPOLIS, MARYLAND**

### **Notes to Basic Financial Statements, Continued**

#### **(1) Summary of Significant Accounting Policies, Continued**

The government-wide Statement of Activities presents a comparison between expenses, both direct and indirect, and program revenues for each segment of the business-type activities of the City and for each governmental program. Direct expenses are those that are specifically associated with a service, program or department and are therefore clearly identifiable to a particular function. Indirect expenses for centralized services and administrative overhead are allocated among the programs, functions and segments using a full cost allocation approach and are presented separately to enhance comparability of direct expenses between governments that allocate direct expenses and those that do not. Program revenues include charges paid by the recipients of the goods or services offered by the programs and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues not classified as programs revenues are presented as general revenues. The comparison of program revenues and expenses identifies the extent to which each program or business segment is self-financing or draws from the revenues of the City.

Net assets should be reported as restricted when constraints placed on net asset use are either externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or imposed by laws through constitutional provisions or enabling legislation. The net assets restricted for other purposes result from special revenue funds and the restrictions on their net asset use.

Separate financial statements are provided for governmental funds, propriety funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements. In addition, the special revenue fund, a non-major individual governmental fund, is reported as a separate column.

#### **FUND FINANCIAL STATEMENTS**

Fund financial statements report detailed information about the City. The focus of governmental and enterprise fund financial statements is on major funds rather than reporting funds by type. Each major fund is presented in a separate column. Non-major funds are aggregated and presented in a single column except for the special revenue fund which is presented in a separate column. The internal service fund is presented in a single column on the face of the propriety fund statements.

#### **GOVERNMENTAL FUNDS**

All governmental funds are accounted for using modified accrual basis of accounting and the current financial resources measurement focus. Under this basis revenues are recognized in the accounting period in which they become measurable and available. Expenditures are recognized in the accounting period in which the fund liability is incurred, if measurable.

The major and non-major governmental funds are:

General Fund - This is the City's primary operating fund. It is used to account for all financial resources except those required to be accounted for in another fund.

## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (1) Summary of Significant Accounting Policies, Continued

Capital Projects Fund - The Capital Projects Fund is used to account for financial resources and expenditures applied to the construction of capital facilities and major purchased items for all governmental fund types.

Special Revenue Fund - The Special Revenue Fund is used to account for Community Development Block Grants received from the federal government.

#### (C) Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using a current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e. revenues and other financing sources) and decreases (i.e. expenditures and other financing uses) in net current assets. The unreserved fund balance is a measure of available spendable resources.

The modified accrual basis of accounting is followed by the governmental funds. Under this basis, revenues are recorded when susceptible to accrual, i.e., both measurable and available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Expenditures are recorded for decreases in net financial resources when a fund liability is incurred, if measurable, except for debt service, which is recognized when due.

Property taxes levied during the current year are recorded as receivables and deferred revenue, net of estimated uncollectible amounts. The net receivables collected during the current year and within sixty days after year end are recognized as revenues in the current year.

Licenses and permits, charges for non-enterprise services, fines and forfeitures and miscellaneous revenues (except investment earnings) are recorded as revenues when received in cash because they are generally not measurable until actually received. Investment earnings are recorded as earned since they are measurable and available.

In applying the susceptible to accrual concept to intergovernmental revenues, the legal and contractual requirements of the numerous individual programs are used as guidance. There are, however, essentially two types of these revenues. In one, monies must be expended on the specific purpose or project before any amounts will be paid to the City; therefore, revenues are recognized based upon the expenditures recorded. In the other, monies are virtually unrestricted as to purpose of expenditure and are usually revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenues at the time of receipt or earlier if the susceptible to accrual criteria are met.

#### **PROPRIETARY FUNDS**

All proprietary funds are accounted for using the accrual basis of accounting. The accrual basis of accounting recognizes revenues when they are earned and expenses when liabilities are incurred. These funds account for operations that are primarily financed by user charges. All proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the balance sheet. Net assets (i.e., net total assets)

## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (1) Summary of Significant Accounting Policies, Continued

are segregated into invested in capital assets, net of related debt, restricted and unrestricted. Propriety funds operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net assets. In accordance with GASB Statement No. 20, "Accounting and Financial Reporting for Propriety Funds and other Governmental Entities that use Propriety Fund Accounting," the City has elected not to follow any pronouncements issued by the Financial Accounting Standards Board since November 30, 1989.

Propriety funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and delivering goods in connection with a propriety funds principal ongoing operations. The principal operating revenues of all the City's enterprise funds and internal service fund are charges to customers for sales and services. Operating expenses for enterprise funds and internal service funds include the cost of sales and services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

The major propriety funds are:

**Water Fund** - To account for all financial activity associated with the operation of the City's water plant and water distribution system. The water plant is responsible for the production, treatment, testing, storage and initial distribution of all potable water for the customers of the City. The water distribution division is responsible for meter reading and operating, maintaining and repairing the distribution system.

**Sewer Fund** - To account for all financial activity associated with the operation of the City's sewage collection and treatment program. The sewer fund consists of two divisions: sewer plant and sewer collection. The sewer collection division is responsible for operating, maintaining and repairing the sewage conveyance system. Sewage treatment is performed at a single, jointly-owned plant site controlled and operated by Anne Arundel County. The City has a fifty percent ownership of the property, plant and equipment but does not have joint control of the financial or operating policies, thus the arrangement is not considered a joint venture. The current agreement calls for the City to share in actual costs for fifty percent of capital improvements and a flow-based percentage of operational costs.

**Off Street Parking Fund** - To account for all financial activity associated with the operations of the City's municipal off street parking facilities. The parking facilities include two parking garages and two parking lots.

Other propriety funds shown separately are:

**Transportation Fund** - To account for all financial activity associated with the operation and maintenance of the City's public transportation system. The transportation fund consists of three divisions: Administration, Transit Operations and Maintenance.

**Refuse Fund** - To account for all financial activity associated with the operation of the City's residential refuse, yard waste, recycling and bulk disposal systems. The refuse fund consists of three divisions:

Residential Refuse, Yard Waste Recycling and Curbside Recycling.

## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (1) Summary of Significant Accounting Policies, Continued

The City's only Internal Service Fund is used to account for the activities of a self-insurance program for general and automotive liability claims. The liability for unpaid claims, which is included in other liabilities, is based upon individual case estimates reported as of June 30, 2003 and management's estimate of claims incurred but not reported to that date.

When both restricted and unrestricted resources are available for use, it is the government's policy to use restricted resources first, and then unrestricted resources as they are needed.

#### **FIDUCIARY FUND - PENSION TRUST FUND**

The City currently has one fiduciary fund. The Pension Trust Fund is used to account for pension assets held by the City in a trustee capacity. This fund is accounted for and reported in a manner similar to proprietary funds since capital maintenance is critical.

#### (D) Change in Accounting principles

The accompanying financial statements of the City have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). In June 1999, the GASB issued Statement 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. These statements establish new financial reporting requirements for state and local governments throughout the United States. They require new information and restructure much of the information that governments have presented in the past. Comparability with reports issued in prior years is affected.

The City is required to implement these standards for the fiscal year ended June 30, 2003. Accordingly, the City has adopted the provisions of GASB 34 for its fiscal year ended June 30, 2003. With the implementation of GASB Statement 34, the City has prepared required supplementary information titled *Management's Discussion and Analysis*, which precedes the basic financial statements.

Other GASB Statements are required to be implemented in conjunction with GASB Statement 34. Therefore, the City has implemented the following GASB Statements in the current fiscal year: Statement 36, *Recipient Reporting for Certain Shared Nonexchange Revenues*, Statement 37, *Basic Financial Statements - and Management Discussion and Analysis - for State and Local Governments: Omnibus*, Statement 38, *Certain Financial Statement Note Disclosures*, Statement 41, *Budgetary Comparison Schedules - Perspective Differences*, and Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*. Beginning balances of net assets were restated to reflect the changes in accounting principles.

The accompanying financial statements are presented as of June 30, 2003, and for the year then ended and present the financial position of the City and the various funds and fund types, the changes in financial position of the City and the various funds and fund types, and the cash flows of the propriety funds.

## **CITY OF ANNAPOLIS, MARYLAND**

### **Notes to Basic Financial Statements, Continued**

#### **(1) Summary of Significant Accounting Policies, Continued**

##### **(E) Budgetary Process**

The City follows these procedures in establishing its budgetary data for the General Fund, Capital Projects Fund, and Enterprise Funds.

- (1) By the second Monday in April, the Mayor submits to the City Council a proposed budget for the General Fund and each of the enterprise funds for the fiscal year commencing the following July 1.
- (2) The budget is referred to the Finance Committee, which makes recommendations on the budget to the full City Council by the second Monday in May.
- (3) The City Council holds public hearings to obtain taxpayer comments.
- (4) No later than June 30, the budget is legally enacted through passage of a budget ordinance which establishes spending authority by fund for the operations of the City.
- (5) Supplemental appropriations and transfers between funds must be approved by the City Council. The allocation of funds from the surplus of the budget requires a two-thirds vote by the City Council.

All budgets are on an annual basis except the Capital Projects Fund budget which is on a project basis. Budgets are adopted using the same basis of accounting as used for reporting purposes, except that for governmental funds, encumbrances are treated as expenditures. Unencumbered appropriations lapse at June 30 for all funds, except the Capital Projects Fund.

##### **(F) Investments**

Short-term investments of the City are recorded at fair value. Investments in the Pension Trust Fund represent the pension plan's ownership interests in the net assets of various investment funds. The investments in these funds are recorded at fair value.

##### **(G) Inventories**

Inventories consist of supplies and materials valued at cost using the first-in/first-out method and are recorded as expenditures/expenses as the items are used.

##### **(H) Capital Assets and Depreciation**

The accounting and reporting treatment applied to the capital assets associated with a fund are determined by its measurement focus. General capital assets are long-lived assets of the City as a whole. When purchased, such assets are recorded as expenditures in the governmental funds and capitalized. Infrastructure such as streets, traffic signals and signs are capitalized. The valuation bases for general capital assets are historical cost, or where historical cost is not available, estimated historical cost based on replacement cost. The minimum capitalization threshold is any individual item with a total cost greater than \$5,000 and a useful life of more than one year.

## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (1) Summary of Significant Accounting Policies, Continued

Capital assets in the propriety funds are capitalized in the fund in which they are utilized. The valuation bases for propriety fund capital assets are the same as those used for the general capital assets. Donated capital assets are capitalized at estimated fair market value on the date donated.

Depreciation of capital assets is computed and recorded by the straight-line method. Estimated useful lives of the various classes of depreciable capital assets are as follows: building, 20 to 50 years; improvement/infrastructure, 5 to 50 years; and equipment, 2 to 15 years.

#### (I) Vacation and Sick Leave

Vacation benefits are earned by employees of the City based on time in service, and the rights to such benefits are vested. Sick leave is also accumulated by employees based on time in service. Accumulated sick leave benefits do not vest and are not paid unless sickness causes employees to be absent; however, accumulated sick time not used is credited to months of service in the calculation of employees' retirement benefits.

The City records vested vacation benefits as earned. The amount earned and unused is recorded as a liability in the respective funds since the City estimates that the entire amount is current. In accordance with GASB Statement Number 16, "Accounting for Compensated Absences," the City also recorded the related social security and medicare taxes as a liability as of June 30, 2003.

#### (J) Cash Flows

For purposes of the statement of cash flows, highly liquid investments with a maturity of three months or less when purchased are considered to be cash equivalents.

#### (K) Designations of Fund Balance

Designations of fund balance represent tentative management plans that are subject to change.

#### (L) New Accounting Pronouncement

In May 2002, GASB issued Statement No. 39, *Determining Whether Certain Organizations Are Component Units*. This statement provides additional guidance to determine whether certain organizations for which the primary government is not financially accountable should be reported as component units by the primary government. This pronouncement requires reporting as a component unit, a fundraising organization which exists for the primary benefit of the primary government or its component units. The City is in the process of assessing the impact of this statement and will implement it as of the effective date.

## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (2) Differences Between GAAP and Budget Basis

The basic financial statements and notes conform with GAAP, which provides that the Statement of Revenues and Expenditures and Encumbrances - Budget and Actual - General Fund (Budget Basis) should be prepared on a budget basis for the governmental funds that are budgeted annually. The statement is also designed to demonstrate compliance and non-compliance with budget limitations. In the General Fund, the budget basis differs from GAAP in that the budget basis reflects encumbrances as the equivalent of expenditures. GAAP reflects encumbrances only as reservations of fund balance. Also, interfund transfers are considered as the equivalent of revenues and expenditures of the affected funds under the budget basis. In addition, new capital leases are recorded as an expenditure and as an other financing source only on a GAAP basis. The GAAP and budget basis statements for the General Fund are reconciled as follows:

	Excess (deficiency) of revenues and other sources over expenditures and other uses
Budget basis	(\$4,505,992)
Effect of encumbrances	<u>484,299</u>
GAAP basis	<u><u>(\$4,021,693)</u></u>

#### (3) Property Tax

The City's real property tax is levied each July 1 on the assessed values certified as of that date for all taxable real property located in the City. At that time, a lien is placed against the property. Assessed values are established by the State Department of Assessments and Taxation at predetermined percentages of estimated market value. A revaluation of all property is required to be completed every three years. Payments are due by September 30. Beginning October 1, interest is charged each month or fraction thereof until such taxes are paid. Delinquent taxes are collected, after the ninth month of delinquency, by tax sales conducted by Anne Arundel County. The assessed market value of taxable real property as of July 1, 2002 was approximately \$2,635,596,635.

#### (4) Cash and Investments

The City maintains an investment pool that is available to all funds except the Pension Trust Fund, which holds investments separate from other City funds and controls its own cash transactions. All other City cash receipt and disbursement transactions are initiated in the General Fund and amounts applicable to other funds are transferred through the respective interfund receivable and payable accounts. The cash balance of the Internal Service Fund is maintained in a separate account at the Maryland Local Government Investment Pool.

At year-end, the carrying amount of the City's deposits was \$37,939 and the bank balance was \$691,198. The bank balance at year-end was covered by federal depository insurance of \$142,144 and by collateral of \$549,076 held by the banks' trust departments in the name of the City. Statutes require the pledging of collateral by the respective banks' trust departments for any uninsured deposits of the City.



## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (4) Cash and Investments, continued

Except for investments in the Pension Trust Fund, the City is authorized to invest in obligations of the U. S. Treasury, agencies and instrumentalities, bankers' acceptances, repurchase agreements, certificates of deposit, and the state's local government investment pool. Contractually, the City's Pension Trust investment managers are restricted to investments in common stock, public bonds, real estate and money market investment funds.

The City's investments at June 30, 2003 are summarized below to give an indication of the level of risk assumed by the City at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by the City or its agent in the City's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the counter-party's trust department or agent in the City's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in the City's name.

	Category			Carrying
	1	2	3	Value
Investments in the state's local government investment pool				\$37,453,319
Investments in pooled investment funds managed by pension trustee				118,995,110
Total				<u>\$156,448,429</u>

The above categorization is representative of the level of risk assumed by the City related to investments throughout the year. Investments in the state's local government investment pool are categorized under cash and cash equivalents since the pool is a demand account that can be accessed for deposits and withdrawals on a daily basis. The Maryland Local Government Investment Pool (Pool) was established under Article 95, Section 22G of the Annotated Code of Maryland and is under the administrative control of the State Treasurer. Mercantile-Safe Deposit and Trust Company is currently contracted to operate the Pool and may invest in any instrument permitted by Section 6-222 of the State Finance and Procurement Article. The City's fair value position in the Pool is the same as the value of pool shares.

#### (5) Liability for Unpaid Claims

The accrued payables and other liabilities of the City's Internal Service Fund consisted of a \$235,083 liability for estimated unpaid claims and \$3,479 of other accrued liabilities, for a total of \$238,562.

# CITY OF ANNAPOLIS, MARYLAND

## Notes to Basic Financial Statements, Continued

### (6) Capital Assets and Depreciation

Capital asset activity for the year ended June 30, 2003 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Governmental activities:				
Not being depreciated:				
Land	\$ 4,099,953	\$ -	\$ -	\$ 4,099,953
Construction in process	6,400,670	5,064,278	(1,840,590)	9,624,358
Subtotal	10,500,623	5,064,278	(1,840,590)	13,724,311
Other capital assets:				
Buildings	13,039,418	14,015	-	13,053,433
Improvements/infrastructure	35,536,152	821,011	-	36,357,163
Equipment	9,020,244	766,012	(269,031)	9,517,225
Subtotal	57,595,814	1,601,038	(269,031)	58,927,821
Accumulated depreciation:				
Buildings	(10,226,543)	(85,124)	3,560	(10,308,107)
Improvements/infrastructure	(28,377,685)	(182,529)	-	(28,560,214)
Equipment	(6,049,522)	(465,711)	278,045	(6,237,188)
Subtotal	(44,653,750)	(733,364)	281,605	(45,105,509)
Net capital assets	\$23,442,687	\$5,931,952	(\$1,828,016)	\$27,546,623

Depreciation was charged to functions as follows:

Governmental activities:

General government	\$45,916
Public safety	336,701
Community services	87,143
Public works	263,604
Total governmental activities depreciation expense	\$733,364

# CITY OF ANNAPOLIS, MARYLAND

## Notes to Basic Financial Statements, Continued

### (6) Capital Assets and Depreciation, Continued

	Beginning Balance	Increases	Decreases	Ending Balance
Business-type activities:				
Not being depreciated:				
Land	\$ 3,243,442	\$ -	\$ -	\$ 3,243,442
Construction in process	5,388,891	5,648,801	(7,473,061)	3,564,631
Subtotal	<u>8,632,333</u>	<u>5,648,801</u>	<u>(7,473,061)</u>	<u>6,808,073</u>
Other capital assets:				
Buildings	25,980,877	5,814,108	-	31,794,985
Improvements/infrastructure	24,022,934	1,097,577	-	25,120,511
Equipment	6,857,922	810,528	(46,404)	7,622,046
Subtotal	<u>56,861,733</u>	<u>7,722,213</u>	<u>(46,404)</u>	<u>64,537,542</u>
Accumulated depreciation:				
Buildings	(10,413,245)	(874,581)		(11,287,826)
Improvements/infrastructure	(9,709,682)	(471,816)		(10,181,498)
Equipment	(4,829,424)	(632,201)	24,743	(5,436,882)
Subtotal	<u>(24,952,351)</u>	<u>(1,978,598)</u>	<u>24,743</u>	<u>(26,906,206)</u>
Net capital assets	<u>\$40,541,715</u>	<u>\$11,392,416</u>	<u>(\$7,494,722)</u>	<u>\$44,439,409</u>

Depreciation was charged to functions as follows:

Business-type activities:

Water	\$451,372
Sewer	658,490
Off street parking	252,959
Other	615,777
Total business-type activities depreciation expense	<u>\$1,978,598</u>

### (7) Debt

The City issues general obligation bonds to provide funds for the acquisition and construction of major capital facilities. General obligation bonds have been issued for both governmental and business-type activities. These bonds therefore are reported in the proprietary funds if they are expected to be repaid from proprietary fund revenues. In addition, general obligation bonds have been issued to refund general obligation bonds. General obligation bonds are direct obligations and pledge the full faith and credit of the City. The City also participates in the Maryland Local Government Insurance Trust, a public entity risk pool, which provides insurance for claims in excess of coverage provided by the City's self-insurance fund. In 1990, Certificates of Participation were issued by the trust with the City's share being approximately 2% of the total. All debt service payments are made from the Trust's fund balance and are due annually to 2009.

# CITY OF ANNAPOLIS, MARYLAND

## Notes to Basic Financial Statements, Continued

### (7) Debt, continued

In fiscal year 2003, the City defeased the callable portion of certain series of general obligation bonds by placing the proceeds of the refunding bonds in an irrevocable trust to provide for all future debt service payments on the refunded bonds. The resulting gain is being added to the new debt and amortized over the remaining life of the refunded debt. The refunding resulted in a net present value savings of \$649,783. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the City's financial statements. At June 30, 2003, \$13,775,000 of bonds defeased are outstanding.

Under provisions of Article 41, Section 14-101 through 14-109 of the Annotated Code of Maryland, the City has participated in Economic Development Revenue Bonds for various projects within the City. Neither the bonds, nor the interest thereon, constitute an indebtedness or contingent liability of the City and, accordingly, they are not included in the basic financial statements. During fiscal year 1998, the City issued \$7,835,000 of these bonds on behalf of St. John's College, a Maryland not-for-profit educational corporation. The aggregate amount of conduit debt outstanding as of June 30, 2003 was \$7,135,000.

During the year, in addition to the refunding bonds, the City issued new debt in the amount of \$20,885,000 for various new construction projects. The following is a summary of changes in long-term liabilities by type of the City for the year ended June 30, 2003:

	Beginning Balance	Additions	Reductions	Unamortized loss on refunding	Ending Balance	Amount due within one year
Governmental Activities:						
General obligation bonds	\$13,173,555	\$13,124,035	(\$4,816,846)	-	\$21,480,744	\$1,812,410
Other debt	170,312	-	(6,250)	-	164,062	6,250
Compensated absences	\$1,585,667	223,501	(34,642)	-	1,774,526	1,774,526
	<u>\$14,929,534</u>	<u>\$13,347,536</u>	<u>(\$4,857,738)</u>	<u>\$0</u>	<u>\$23,419,332</u>	<u>\$3,593,186</u>
Business-type Activities:						
General obligation bonds	\$12,317,488	\$15,450,965	(\$5,048,156)	(\$393,451)	\$22,326,846	\$1,822,580
Other debt	1,146,761	-	(72,291)	-	1,074,470	74,640
Compensated absences	337,853	25,083	(16,516)	-	346,420	346,420
	<u>\$13,802,102</u>	<u>\$15,476,048</u>	<u>(\$5,136,963)</u>	<u>(\$393,451)</u>	<u>\$23,747,736</u>	<u>\$2,243,640</u>

## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (7) Debt, continued

The City is not in violation of any debt agreement provisions. The City Charter limits the aggregate amount of bonds and other indebtedness, with certain exceptions, to 10% of the assessable base of the City, which includes real and personal property. At June 30, 2003, the debt margin of the City was as follows:

Assessable basis upon which tax levy for year beginning July 1, 2002 was calculated	<u>\$2,786,719,148</u>
Debt limit; 10% of assessable basis	278,671,915
Debt subject to limitation	<u>32,715,169</u>
Debt margin	<u>\$245,956,746</u>

Long-term debt amounts are comprised of the following as of June 30, 2003:

#### Governmental activities:

##### General obligation bonds:

Public Improvements Bonds of 1993: \$697,734; interest 3.6% to 5.5%; due serially to 2013	\$33,215
Public Improvements and Refunding Bonds of 1994: \$3,941,632; interest 3.3% to 5.9%; due serially to 2015	1,624,438
Public Improvements Bonds of 1995: \$3,883,340; interest 4.8% to 6.8%; due serially to 2015	309,716
Public Improvements and Refunding Bonds of 1998: \$9,862,595; interest 4.375% to 5%; due serially to 2017	6,389,340
Public Improvements Bonds of 2002: \$9,552,799; interest 2.5% to 5%; due serially to 2018	9,552,799
Refunding Bonds of 2003: \$3,571,236; interest 2.65% ; due serially to 2015	3,571,236

##### Other debt:

State of Maryland - MICRF loan: \$250,000; no interest; due quarterly to 2004	<u>164,062</u>
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Total governmental activities long-term debt	<u>\$21,644,806</u>
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## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (7) Debt, Continued

##### Business-type activities:

##### General obligation bonds

Public Improvements Bonds of 1993: \$2,977,266; interest 3.6% to 5.5%; due serially to 2013	\$141,785
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Public Improvements and Refunding Bonds of 1994: \$3,503,368; interest 3.6% to 5.9%; due serially to 2015	1,084,141
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Public Improvements Bonds of 1995: \$1,771,660; interest 4.8% to 6.8%; due serially to 2015	195,284
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Public Improvements and Refunding Bonds of 1998: \$9,352,405; interest 4.375% to 5%; due serially to 2017	5,880,092
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Public Improvements Bonds of 2002: \$11,332,201; interest 2.5% to 5%; due serially to 2018	11,332,201
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Refunding Bonds of 2003: \$4,118,764; interest 2.65% ; due serially to 2015	3,693,343
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##### Other debt:

State of Maryland Water Quality loan: \$1,570,795; interest 3.25% payable from net cash provided by operations of sewer as generated	1,074,470
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Total business-type activities debt	<u><u>\$23,401,316</u></u>
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Interest costs incurred on general obligation bonds allocated to the business-type activities were \$743,315 for the year ended June 30, 2003.

# CITY OF ANNAPOLIS, MARYLAND

## Notes to Basic Financial Statements, Continued

### (7) Debt, Continued

Long-term debt maturities excluding the unamortized loss on refunding of \$662,409 in business-type activities are scheduled as follows:

	General obligation bonds		Other debt		Total
	Principal	Interest	Principal	Interest	
Governmental activities:					
2004	1,812,410	821,534	6,250	-	2,640,194
2005	1,870,190	769,003	157,812	-	2,797,005
2006	1,733,449	698,145	-	-	2,431,594
2007	1,822,212	617,446	-	-	2,439,658
2008	1,607,345	555,424	-	-	2,162,769
2009-2013	7,342,932	1,878,932	-	-	9,221,864
2014-2018	5,292,206	622,254	-	-	5,914,460
	<u>\$21,480,744</u>	<u>5,962,738</u>	<u>164,062</u>	<u>\$0</u>	<u>27,607,544</u>
Business-type activities					
2004	1,822,580	862,337	74,640	34,920	2,794,477
2005	1,764,810	818,310	77,066	32,495	2,692,681
2006	1,741,551	755,940	79,571	29,990	2,607,052
2007	1,887,788	675,369	82,157	27,404	2,672,718
2008	1,747,655	611,925	84,827	24,734	2,469,141
2009-2013	8,107,068	2,084,006	467,324	80,479	10,738,877
2014-2018	5,917,803	693,808	208,885	10,237	6,830,733
	<u>\$22,989,255</u>	<u>6,501,695</u>	<u>1,074,470</u>	<u>240,259</u>	<u>30,805,679</u>

### (8) Pension Plans

Generally, all regular City employees, except policemen and firemen, participate in the Employees Retirement and Pension Systems (Systems), cost sharing multiple-employer defined benefit plan sponsored and administered by the State Retirement and Pension System of Maryland. Police and fire personnel participate in a single employer defined benefit pension and disability plan, which is administered by the City's personnel director. In addition, the City established an eight-member police and fire retirement plan commission to review funding and actuarial reports and to make investing decisions. The City Council has the authority to establish and amend benefit and contribution provisions. The Systems were created by the Maryland General Assembly and the Police and Fire System was established by City legislation.

## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (8) Pension Plans, Continued

##### Plan Description and Contribution Information

##### (A) Cost Sharing Multiple-Employer Plan

The Systems provide retirement, disability, and death benefits to participants and their beneficiaries. The State Retirement and Pension System of Maryland issues a publicly available financial report that includes financial statements and required supplementary information. The financial report may be obtained by writing to State Retirement Agency of Maryland, 301 W. Preston Street, Baltimore, Maryland 21201.

Members of the Retirement System are required to contribute 5% and the City is required to contribute the remaining amount. For the participants in the Pension System, the City contributes 100%. City contributions to the Systems, which were equal to 100% of the required contribution, for the years ended June 30, 2003, 2002, and 2001 were \$504,727, \$427,644, and \$508,083, respectively.

##### (B) Single Employer Plan

The Police and Fire System is a single-employer defined benefit plan that covers the police and fire personnel of the City. The plan provides retirement, disability, and death benefits to its members and beneficiaries. Participants with twenty years of service and hired before August 1, 1972, or those hired between August 1, 1972 and August 1, 1979 and age 55 are eligible for benefits equal to 2% of average earnings times years of service to a maximum of thirty years but no benefits are provided for early retirement. Participants in the revised version of the plan with twenty-five years of service are eligible for benefits equal to 2% of average earnings times years of service to a maximum of thirty-seven and one-half years. Reduced benefits are available under this plan at age 50 with twenty years of service.

Participants in the original plan are required to contribute 3% of their annual salary and the revised plan participants are required to contribute 5% of their annual salary. The City is required to fund the remaining cost of the plan. The City does not calculate a net pension obligation, but develops an annual required contribution as a percent of payroll. The annual pension cost is equal to the annual required contribution. The contribution rate applied to actual payroll is actuarially determined and consists of a normal cost component and an unfunded actuarial liability component. As of July 1, 2002, the normal cost rate was 19.26% and the unfunded actuarial liability rate was a negative 42.92%. As a result of the net negative contribution rate, the City did not have an annual required contribution for the fiscal year ending June 30, 2003. The City had no annual required contribution, but made contributions of \$271,940, \$245,320, and \$236,456 for the fiscal years ending June 30, 2003, 2002, and 2001, respectively. The City has made all the required contributions. Administrative costs of the plan are financed through investment earnings. The plan is considered part of the City's reporting entity and is included in the City's financial statements as Pension Trust funds. There is no separately issued financial report for this plan.



## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (8) Pension Plans, Continued

The number of employees covered and current membership classification as of July 1, 2002 are as follows:

Non-Active Members:

Retirees and beneficiaries receiving benefits	131
Terminated employees not yet receiving benefits	21

Active Employees:

Fully vested	22
Non-vested	151

Historical trend information gives an indication of the progress made in accumulating sufficient assets to pay benefits when due and is presented as required supplementary information in the section which follows the "Notes to Financial Statements" section.

#### (9) Other Post Retirement Benefits

The City allows retired employees to participate in its group health insurance plan. The full cost is paid by the employee.

#### (10) Interfund Receivables and Payables

Interfund receivables and payables, which are for temporary balances between other funds and the general fund where cash is pooled, consist of the following at June 30, 2003:

	Receivables	Payables
General Fund:		
Internal Service Fund	1,151,223	-
Enterprise Funds:		
Transportation Fund	2,487,191	-
Internal Service Fund:		
General Fund	-	1,151,223
Enterprise Funds:		
General Fund	-	2,487,191
Pension Trust Fund:		
	<u>\$3,638,414</u>	<u>3,638,414</u>

## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (10) Interfund Receivables and Payables, Continued

The City allocates interest between the General and enterprise funds based upon month-end interfund balances at the average monthly interest rate of the state's local government investment pool. Such allocation for the year ended June 30, 2003 is reported as an interfund credit in the General Fund and as a portion of the administrative charge from General Fund in the enterprise funds.

#### (11) Contingencies

The City, in the normal course of activities, is a defendant in several lawsuits. Losses, if any, are estimated to be less than the City's insurance coverage. Potential liabilities are covered by the City's self-insurance fund and the City's participation in the Maryland Local Government Insurance Trust, a public entity risk pool.

#### (12) Capital Facilities and Connection Charges

In the enterprise funds, capital facility charges are assessed to property owners over a period of thirty years from the date related properties physically connect to the City's water and/or sanitary sewage collection and treatment systems. Such charges are legally restricted to pay for capital construction within the systems or to pay for debt service on debt issued to finance such construction. As such construction is typically financed with debt, the City recognizes the annual charges earned as an addition to contributed capital. Charges levied and receivable in future years are reported as a receivable and deferred revenue.

A connection charge not exceeding the cost of connecting to the systems is assessed and collected prior to connection. Such revenue is recognized as operating income and recorded as charges for services.

#### (13) Construction Commitments

As of June 30, 2003, the City had a \$325,000 commitment for renovations to the police department, \$1,434,000 for road improvements, \$1,400,000 for a comprehensive municipal software installation, and \$1,237,000 for new vehicle purchases. Subsequent to year end, the City entered into commitments of \$1,729,000 for additional road improvements and \$6,465,000 for a new parking garage.

#### (14) Grants

The City receives grants from time-to-time. Expenditures from certain grants are subject to audit by the grantor, and the City is contingently liable to refund amounts received in excess of allowable expenditures. In the opinion of the City's management, no material refunds will be required as a result of disallowed expenditures.

#### (15) Risk Management

The City is exposed to various risks of loss related to torts; thefts of, damage to, and destruction of assets; errors and omissions; injuries to workers; and natural disasters. The City maintains a self-insurance fund and participates in the Maryland Local Government Insurance Trust, a public entity risk pool, which provides insurance for claims in excess of coverage provided by the City's self-insurance fund.

## CITY OF ANNAPOLIS, MARYLAND

### Notes to Basic Financial Statements, Continued

#### (15) Risk Management, Continued

This is a total risk and cost sharing pool for all participants. In the event that the Trust's General Fund falls into a deficit that cannot be satisfied by transfers from the Trust's capital and surplus accounts, the Trustees shall determine a method to fund the deficit. The Trust agreement empowers the Trustees to assess an additional premium to each deficit-year participant. Debt issues could also be used to fund a deficit.

Premiums are charged to the City's General Fund, with no provision made for claim liability in addition to premiums, unless an assessment is made by the Trust. There have been no assessments during the year ended June 30, 2003.

The City accounts for the financial operations of the self-insurance fund in the Internal Service Fund. The City maintains excess coverage to reduce the exposure from catastrophic claims. A third party insurance administrator is employed to estimate funding requirements and liabilities of the self-insurance fund. The funding for each year represents the present value of the amount needed to pay the expected final settlement values for all claims which occur in that year regardless of the date reported. Claims "incurred but not reported" are accounted for as accrued payables and other liabilities in the Internal Service Fund in accordance with GASB No. 10 and FASB No. 5, as applicable. The carrying amount of liabilities for unpaid claims is presented at present value using a discount rate of 4% to recognize the time value of money. The changes in accrued payables and other liabilities during fiscal years 2002 and 2003 were as follows:

	FY 2002	FY 2003
Beginning accrued payables and other liabilities	\$359,061	\$235,841
Incurred claims and changes in estimates	140,594	153,610
Claim payments	(263,814)	(150,889)
Ending accrued payables and other liabilities	<u>\$235,841</u>	<u>\$238,562</u>

There have been no reductions in insurance coverage from the prior year and during the last three years the total amount of settlements has not exceeded insurance coverage.

#### (16) Landfill Closure

In accordance with the Maryland Department of the Environment regulations, as of June 30, 1993, the City's landfill operations were terminated. As of March 31, 1998, the landfill is closed with closure and postclosure costs recorded under current Federal and State regulations. The City will continue the monitoring process per the regulations and currently plans to maintain the site as open space. Actual costs may be higher due to inflation, changes in technology, or changes in regulations. An annual appropriation is established for the monitoring costs and any postclosure care requirements exceeding the original estimates will be covered by future tax revenues.

**CITY OF ANNAPOLIS, MARYLAND**  
**REQUIRED SUPPLEMENTARY INFORMATION**  
PENSION FUND  
(Unaudited)

**SCHEDULES OF FUNDING PROGRESS**

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	Unfunded AAL as a Percentage of Covered Payroll ((b-a)/c)
7/1/97	\$ 84,665,065	\$ 77,319,805	\$ (7,345,260)	109%	\$ 9,364,421	(78)%
7/1/98	99,032,147	80,099,248	(18,932,899)	124%	9,025,836	(210)%
7/1/99	112,085,087	85,554,792	(26,530,295)	131%	9,558,356	(278)%
7/1/00	120,904,575	91,865,741	(29,038,834)	132%	9,846,570	(295)%
7/1/01	126,970,542	94,675,422	(32,295,120)	134%	10,004,140	(323)%
7/1/02	127,869,748	95,634,091	(32,235,657)	134%	10,553,804	(305)%

A negative Unfunded Actuarial Accrued Liability represents a funding excess.

**SCHEDULES OF EMPLOYER CONTRIBUTIONS**

Fiscal Year	Annual Required Contribution	Employer Contribution	Percentage Contributed
1997	\$ 766,985	\$ 840,892	110%
1998	234,899	780,261	332%
1999	-	231,587	N/A
2000	-	245,928	N/A
2001	-	236,456	N/A
2002	-	245,320	N/A
2003	-	271,940	N/A

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows.

Actuarial valuation date	7/1/02
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	10 years - open
Asset valuation method	Asset smoothing
Actuarial assumptions:	
Investment rate of return	7.5% compounded annually
Projected salary increases	6.0% compounded annually
Cost of living adjustments	5.0% compounded annually
Inflation rate	5.0%
Contribution rates:	
City	0%
Members	3 - 5%